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JUL 29 2002

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

July 29, 2002

Via HAND DELIVERY

Ms. Marlene H. Dortch
Secretary
Federal Communications Commission
The Portals – TW-A325
445 Twelfth Street, S.W.
Washington, D.C. 20554

Re: MB Docket No. 02-145

Dear Ms. Dortch:

On behalf of EchoStar Satellite Corporation ("EchoStar"), enclosed please find for filing an original and four copies of EchoStar's Comments in the above-referenced proceeding.

Also enclosed is an additional copy of EchoStar's Comments which we ask you to date-stamp and return with our messenger.

If you have any questions, please do not hesitate to contact me.

Sincerely,

Rhonda M. Bolton

Rhonda M. Bolton
Counsel for EchoStar
Satellite Corporation

Enclosures

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JUL 29 2002

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
	)	
Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming	)	MB Docket No. 02-145

COMMENTS OF ECHOSTAR SATELLITE CORPORATION

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July 29, 2002

SUMMARY

Despite the continued growth of DBS subscribership, truly effective competition in the multi-channel video programming distributor ("MVPD") market has yet to arrive. Moreover, cable's grip on the MVPD market is tightening. Through consolidation, clustering, digital and broadband bundling, and in some cases the outright refusal of their affiliates to sell programming to competitors, the cable companies are systematically maintaining their immense market power. These actions have resulted, despite the limited success of DBS in acquiring subscribers, in an increase of 45%, nearly three times the rate of inflation, in cable rates since the passage of the 1996 Telecommunications Act.[1] While DBS is the best hope of imposing competitive discipline on the small club of MSOs that control the majority of U.S. pay television households, if recent trends continue, DBS will be less able to offer a competitive alternative to cable, resulting in even higher cable rates and more overt anticompetitive behavior. Only through the combined resources of the two major DBS providers, EchoStar and DIRECTV, will the DBS industry be able to compete effectively in the future against cable. In fact, the EchoStar-Hughes merger will generate more than an estimated $1 billion per year in consumer welfare benefits. These benefits will flow to existing DBS subscribers *and* cable subscribers who will reap the rewards of increased competition from, for example, the introduction of DBS local broadcast service in every designated market area, a direct result of the merger.

[1] "Abusing Consumers and Impeding Competition: The State of the Cable Television Industry, 2002" at 2, Chris Murray, Gene Kimmelman, and Dr. Mark Cooper, Consumers Union, July 24, 2002, available at http://www.consumersunion.org/pdf/cable2002.pdf (last visited July 29, 2002) ("*Consumers Union Cable Report*").

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COMMENTS OF ECHOSTAR SATELLITE CORPORATION

EchoStar Satellite Corporation ("EchoStar") hereby submits its Comments in the above-captioned proceeding. EchoStar is a multi-channel video programming distributor (MVPD) providing Direct Broadcast Satellite (DBS) service to subscribers throughout the United States. It currently operates seven DBS satellites and plans to launch additional satellites in the near future. As of March 21, 2002, EchoStar's DISH Network served more than 7.165 million households.

Despite the continued growth of DBS subscribership, truly effective competition in the multi-channel video programming distributor ("MVPD") market has yet to arrive. Moreover, cable's grip on the MVPD market is tightening. Through consolidation, clustering, digital and broadband bundling, and in some cases the outright refusal of its affiliates to sell programming to competitors, the cable companies are systematically maintaining their immense market power. These actions have resulted, despite the limited success of DBS in acquiring subscribers, in an increase of 45%, nearly three times the rate of inflation, in cable rates since the passage of the 1996 Telecommunications

Act.[1] While DBS is the best hope of imposing competitive discipline on the small club of MSOs that control the majority of U.S. pay television households, if recent trends continue, DBS will be less able to offer a competitive alternative to cable, resulting in even higher cable rates and more overt anticompetitive behavior. Only through the combined resources of the two major DBS providers, EchoStar and DIRECTV, will the DBS industry be able to compete effectively in the future against cable. In fact, the EchoStar-Hughes merger will generate more than an estimated $1 billion per year in consumer welfare benefits. These benefits will flow to existing DBS subscribers *and* cable subscribers who will reap the rewards of increased competition from, for example, the introduction of DBS local broadcast service in every designated market area ("DMA"), a direct result of the merger.

I. THE CABLE COMPANIES' ENTRENCHED DOMINANT MARKET POWER WILL PERSIST WITHOUT A STRENGTHENED DBS PLATFORM

The Commission must reach the same conclusion in the ninth competition report that it did in the first: cable television remains the dominant MVPD platform. Whether measured in market share, pricing behavior, market foreclosure, or other indicators of market power, the cable companies have retained their dominant position. DBS is the best hope for imposing competitive discipline on cable, but must be allowed to grow stronger if it is to sustain a viable threat.

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[1] "Abusing Consumers and Impeding Competition: The State of the Cable Television Industry, 2002" at 2, Chris Murray, Gene Kimmelman, and Dr. Mark Cooper, Consumers Union, July 24, 2002, available at http://www.consumersunion.org/pdf/cable2002.pdf (last visited July 29, 2002) ("*Consumers Union Cable Report*").

a. Cable remains the dominant MVPD provider.

The Commission eloquently articulated the degree of cable's dominance in the MVPD market in its recent order extending the prohibition against vertically integrated programmers' exclusive carriage agreements with cable operators. The Commission found that, with 78% of all MVPD subscribers, "cable operators continue to decisively dominate the market for the distribution of [video] programming."[2] Such dominance finds its roots in a market characterized by high concentration and barriers to entry.

Another measure of the cable industry's dominant position in the MVPD market is the ability to increase prices. In the April 2002 *Report on Cable Industry Prices*, the FCC concluded that cable prices rose 7.5 percent during the 12-month period ending on July 1, 2001.[3] For comparison, the Consumer Price Index (CPI-U) increased by 2.7 percent during that same time period. Such price increases far outpacing inflation are also suggestive of the cable industry's ability to exercise significant market power.

The barriers to entry erected by the cable operators include textbook methods of a dominant company bent on using its market power to eliminate competition, including "strategic behavior by incumbent cable operators designed to raise rivals' costs" through refusing to sell regional programming to DBS competitors.[4] With such tactics readily apparent and market share statistics essentially unchanged over a period of years, the

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[2] *Implementation of the Cable Television Consumer Protection and Competition Act of 1992 – Development of Competition and Diversity in Video Programming Distribution: Section 628(c)(5) of the Communication Act: Sunset of Exclusive Contract Prohibition*, FCC 02-176 (June 28, 2002) ("*Program Access Order*") at ¶ 65. *See also id.* at ¶ 47. ("[C]able operators continue to dominate the market for distribution of multichannel video programming with regard to both national and regional programming.")
[3] *Implementation of Section 3 of the Cable Television Consumer Protection and Competition Act of 1992 - Statistical Report on Average Rates for Basic Service, Cable Programming Service, and Equipment*, FCC 02-107 (April 4, 2002) ("*2002 Report on Cable Industry Prices*") at ¶ 4.
[4] *Program Access Order* at ¶ 46 (citing *Annual Status of Competition in the Market for the Delivery of Video Programming*, 17 FCC Rcd. 1244, 1258 ("*Eighth Annual Report*")). *See also infra* Section III regarding cable operators' use of terrestrial delivery to evade program sale requirements.

Commission wisely rejected cable's claims that the competitive landscape had changed sufficiently since 1992 to justify eliminating the exclusivity ban.[5] It similarly should conclude in this proceeding that cable's dominance continues unabated.

b. A stronger DBS competitor will generate significantly more than $1 billion a year in consumer benefits.

Against the backdrop of the dominant cable industry, DBS has been and remains the best hope for infusing competition into the MVPD market, with the potential to bring lower rates and better service to all MVPD consumers. The enactment of the Satellite Home Viewer Improvement Act of 1999 (SHVIA) and the introduction of local-into-local service stimulated DBS growth, and this growth continues today, although at a slower pace than previous years. The data show that cable rates are significantly lower and DBS penetration is significantly higher as a result of the introduction of DBS local-into-local service. The advent of local broadcast carriage by DBS providers has brought a degree of competition against cable operators heretofore unrealized by alternative MVPDs. However, due to spectrum capacity constraints, DBS providers have been able to bring the competitive benefits of local service into only a limited number of DMAs nationwide. The promise of the EchoStar/Hughes combination – local service delivered into every media market in the nation – would bring competition against cable to an entirely new level.

The merger will put significantly more than one billion dollars a year in benefits in the pockets of consumers, of which a significant portion will be due to the introduction

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[5] "We are not persuaded by the arguments presented by cable MSOs, however, that market conditions have changed so fundamentally, and competition in the distribution of video programming is now so robust, that vertically integrated programmers no longer have the incentive to favor affiliated cable operators such that, in the absence of the prohibition, competition and diversity in the distribution of video programming would not be preserved and protected." *Program Access Order* at ¶ 45.

of nationwide local-into-local service alone. Historically, DBS providers' inability to deliver local channels was a severe competitive disadvantage against cable. The Department of Justice concluded that, "to the extent that DBS cannot offer subscribers local broadcast channels, it has a competitive disadvantage relative to cable because many viewers demand local news and weather and popular network programming."[6] Moreover, according to a January 2000 survey by Forrester Research, 47% of cable subscribers would not subscribe to satellite television because they do not "want to lose reception from the major networks (e.g., ABC, NBC, CBS.)"[7]

The addition of local channels has made DBS more competitive with the incumbent cable providers. Indeed, the introduction of local service has led to an increase in DBS subscribership *and* a restraint on cable prices. The importance that consumers place on local channels as part of a DBS offering is clearly demonstrated in the DMAs in which EchoStar and DIRECTV already offer local channels. In those DMAs, the increase in cable prices has been lower than in markets in which DBS does not provide local service. Drs. Willig and Joskow have found that the introduction of local service by DBS lowers the average cable expanded basic price by roughly $1.03 per month in the first year and about $1.57 per month in the second year following introduction of local-into-local service. In other words, where DBS firms become more competitive through the introduction of local broadcast service, not only do DBS

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[6] *See* Comments of the U.S. Department of Justice, *In the Matter of the Application of MCI Telecommunications Corporation and EchoStar Communications Corporation*, File No. SAT-ASG-19981202-00093, January 14, 1999, available at http://www.usdoj.gov/atr/public/comments/2173.htm.
[7] *See* Robert D. Willig, Reply Declaration On Behalf Of Echostar Communications Corporation, General Motors Corporation, and Hughes Electronics Corporation, CS Docket No. 01-348, (filed February 25, 2002), ("Willig Reply Declaration") at ¶ 17.

subscribers benefit from an improved service offering, but cable subscribers experience a favorable impact on the prices they pay.

Taken as a whole, the benefit to cable subscribers through improved DBS service amounts to hundreds of millions of dollars a year saved in cable rates, an amount that will increase significantly if DBS is permitted to offer local service in all DMAs. The consumer welfare benefits from the merger that are relatively easier to quantify are estimated to be significantly greater than $1 billion a year.[8]

c. A stronger DBS competitor will better address cable's broadband and digital offerings.

In its NOI, the Commission seeks comment on the provision of advanced services by the direct-to-home satellite industry.[9] Unfortunately, the state of satellite broadband development is grim. This year, despite over $100 million in investments from EchoStar, Microsoft, and others, EchoStar's satellite broadband partner, Starband Communications, declared bankruptcy.[10] Moreover, Hughes Electronics CEO Jack Shaw told investors that Hughes would be unable to sustain its venture into the consumer satellite broadband market, DIRECWAY, if current financial conditions persisted.[11] Simply put, it is questionable in today's economic climate whether any stand-alone DBS provider can

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[8] *See* Robert Willig and Andrew Joskow, Ex Parte Presentation in CS Docket No. 01-348 on Behalf of EchoStar Communications Corporation, Hughes Electronics Corporation and General Motors Corporation, Analysis of the EchoStar-Hughes Merger: Competitive Effects and National Pricing, July 2, 2002 (filed June 28, 2002) ("Willig and Joskow Competitive Effects Presentation"), at Slide 5 .

[9] *In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, MB Docket No. 02-145 at ¶ 40 (rel. June 14, 2002) ("2002 Notice").

[10] Telecommunications Reports, 2002 WL 20134031, June 10, 2002 ("Satellite-based broadband service provider StarBand Communications, Inc., filed for Chapter 11 bankruptcy protection in federal bankruptcy court in Wilmington, Del.").

[11] Satellite News, Vol. 25, Issue 9, 2002 WL 8254963, March 4, 2002 ("The amount of money that we are spending with our broadband offering does not square with the number of subscribers we are getting.... It is doubtful that Hughes could fund its broadband offering beyond 2002 with the number of subscribers we are serving.").

realistically provide an affordable, competitive, satellite-based two-way high speed Internet broadband service to residential subscribers.

Meanwhile, the cable industry is effectively using cable broadband and digital tier offerings to cement its dominance in the MVPD market.[12] With respect to broadband, cable remains the leading broadband platform in residential areas.[13] By offering a bundled, or in many instances tied, video/broadband product, cable operators are better able to retain and attract subscribers.[14] Digital cable has enabled cable operators to better respond to the advantages of DBS, leading many to conclude that DBS will lose its ability to compete.[15] For example in addition to the broadband/ video bundle that DBS cannot match, digital cable providers are also rolling out true Video-on Demand, localized interactive services and local HDTV programming, none of which can be offered on DBS as presently constituted.

The proposed EchoStar/Hughes merger will help to balance the scales between satellite and cable. Only through combining the customer bases of EchoStar and DIRECTV will the DBS industry be able to develop a consumer broadband offering that is both profitable and attractive to subscribers. EchoStar and Hughes believe that, assuming a level take-rate among existing DBS subscribers of satellite broadband, the

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[12] *See supra,* note 1, *Consumers Union Cable Report* at 10 (commenting that "[c]able has been adding digital subscribers at a much higher rate than [DBS] and is now bundling high-speed Internet with digital service. This is a bundle that [DBS] cannot match.")

[13] *Id.*

[14] "U.S. Cable TV Operators Continue to Jump on the Digital Bandwagon Reports In-Stat/MDR", Business Wire, April 2, 2002 ("Faced with stiff competition from [DBS], the cable television industry is fighting back by focusing on its ability to deliver a "package" of digital services, to include digital video service, cable modem service, and even cable telephony service.").

[15] *See, e.g.*, "Financial Analysts Tell NCTA Cable's Day Will Come Again", Communications Daily, Vol. 22, Issue 89, May 8, 2002 (quoting one financial analyst as saying that "satellite's weaknesses would particularly emerge as battlefront increasingly shifted beyond digital video programming to high-speed data, IP telephony, video-on-demand (VoD) and other advanced digital services.") *See also* Satellite News, The Satellite News Financial Ticker, May 13, 2002 ("the economics of the DBS business model has come under pressure over the past year due to the maturation of the multi-channel TV market and increased competition from cable.").

combined subscriber base would produce the 5 million broadband subscribers necessary to create a profitable and sustainable enterprise. This, in turn, will allow DBS to offer the essential "bundle" of video and data necessary to remain competitive in the MVPD marketplace. In addition, the spectrum reclaimed through the merger will enable the combined DBS entity to offer more programming services, thereby answering cable's digital tier with a stronger offering and further pressuring the cable companies to lower their rates.

II. NON-CABLE HOMES ARE DECREASING IN NUMBER AND SCATTERED

At the same time that cable operators are developing strategies to maintain their market dominance, they are extending their reach among television households in the U.S. Each year, the Commission reports a higher number of homes passed by cable operators, with 104 million homes, or 97.1% of television households, passed by cable last year.[16] Some interested parties have argued that the source of these figures, Paul Kagan Associates, is less accurate than that of Warren Communications, which generally reports a higher number of homes not passed by cable. Given the Commission's history of citing the Kagan data and given the potential flaws in the Warren data, EchoStar recommends that the Commission maintain its past practice of using the Kagan data to identify what percentage of homes are passed by cable.

Drs. Willig and Joskow have pointed out the potential inaccuracies associated with the Warren data. For example, they found that a significant percentage of DIRECTV subscribers who lived in zip codes identified by Warren as not passed by

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[16] *Eighth Annual Report* at ¶ 17.

cable stated they were leaving DIRECTV for a cable provider.[17] A subscriber who leaves a DBS provider for cable cannot be deemed to be living in a non-cable passed household. To confirm that such zip codes were in fact served by cable operators, the independent research firm of Ginsberg Lahey, LLC contacted local cable operators to confirm that they did indeed serve the zip codes identified by Warren as not passed by cable. By directly asking cable operators whether they served these zip codes, Ginsberg Lahey confirmed that a significant number of zip codes identified by Warren as non-cable passed actually were served by a cable operator.

Moreover, the few television households not passed by cable are not concentrated in particular regions or types of locations. Conventional wisdom might suggest that non-cable passed households are concentrated in rural or sparsely populated states. Not so. Cable coverage is geographically dispersed, with some of the smallest communities in the United States showing high percentages of homes passed by cable. For example, Idaho, Iowa, and North Dakota all have 90% or more homes passed by cable. Thus, even if DBS operators had an incentive to charge different prices in the places where cable infrastructure is absent, they could not effectively pinpoint the small number of non-cable passed homes, and they do not do so today. The Commission should conclude that cable's expanding reach heightens the need for a stronger DBS competitor.

III. CABLE OPERATORS HAVE USED TERRESTRIAL DELIVERY OF PROGRAMMING TO CIRCUMVENT PROGRAM ACCESS REQUIREMENTS

The behavior of cable operators is as good as any quantitative measure to demonstrate cable's dominance in the MVPD market. The refusal by certain cable operators to sell their terrestrially delivered programming to DBS operators is a textbook example of a

[17] *See generally supra* note 8, Willig and Joskow Competitive Effects Presentation at Slide 72.

firm using its market power to diminish competition.[18] EchoStar continues to believe that the "loophole" in the existing program access regime, which allows vertically integrated cable programmers to secure exclusive distribution agreements with cable operators for terrestrially delivered programming, harms competition in the MVPD market.[19]

The Commission made several important conclusions in the Program Access Order that demonstrate its understanding of this problem, if not its belief in its own statutory authority to address cable's tactics. The Commission correctly identified the withholding of programming as a method used by cable operators to harm their competition.[20] It stated in no uncertain terms that "vertically integrated programmers, given the opportunity, will foreclose strategic programming, either new or existing, to one or both DBS competitors to undermine their service offering and harm their competitive ability."[21] The Commission also concluded that "terrestrial distribution of programming could have a substantial impact on the ability of competitive MVPDs to compete in the MVPD market."[22]

EchoStar could not agree more. The terrestrial delivery of programming is bound to increase, while at the same time, local and regional programming such as home team sports and local events becomes ever more valued by consumers. Not coincidentally, as

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[18] The refusal of vertically integrated cable MSOs to sell programming to DBS competitors is of course devoid of any legitimate business purpose, and serves only to increase, improperly, the cable firms' power in the MVPD market. *See, e.g., Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585, 608 (1985) (affirming jury finding of Sherman Act violation where defendant failed to show that its refusal to deal "was justified by any normal business purpose").

[19] This view is corroborated in, for example, the *Consumers Union Cable Report* at 11, where the authors cite Comcast's actions in Philadelphia as an example of a cable MSO's exploitation of the terrestrial loophole to its advantage.

[20] *Program Access Order* at ¶ 55 ("The withholding of programming from competitors as a competitive tactic … has been evidenced by the acquisition of … rights in terrestrial-delivered content not covered by the statutory restriction.") (citing *DIRECTV, Inc. v. Comcast Corporation*, 15 FCC Rcd. 22802, 22807 (2000)).

[21] *Program Access Order* at ¶ 60.

[22] *Program Access Order* at ¶ 73.

the Commission found, this is the type of programming the cable operators tend to withhold from DBS.[23] It stands to reason, therefore, that in markets like Philadelphia, where Comcast has refused to sell to DBS operators its terrestrially delivered local sports programming, DBS penetration is well below the national average.[24]

EchoStar believes that no assessment of the state of competition in the MVPD market would be complete without a thorough discussion of cable's use of terrestrial delivery to evade the exclusivity prohibition, a conclusion that such behavior is anticompetitive, and a call to end this blatantly harmful tactic. The Commission should conclude that the "terrestrial loophole" be eliminated either by regulation or act of Congress.

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[23] *Program Access Order* at ¶ 59 ("The evidence suggests that the ability to foreclose vertically integrated programming is especially significant in the regional programming market which may not be covered by the rules if the programming is distributed terrestrially. This type of programming has in fact been withdrawn from DBS competitors.") (citing *Comcast*, 15 FCC Rcd. at 22807.).

[24] *Program Access Order* at n. 107 ("[I]t is apparent that DBS penetration in Philadelphia is well below the 18 percent national penetration rate.").

IV. CONCLUSION

EchoStar urges the Commission to take the foregoing comments into account in its next annual report.

Respectfully submitted,

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